

318



SECUR

05037700

MISSION

OMB APPROVAL
OMB Number: 3235-0123
Expires: January 31, 2007
Estimated average burden hours per response . . . 12.00

2/11

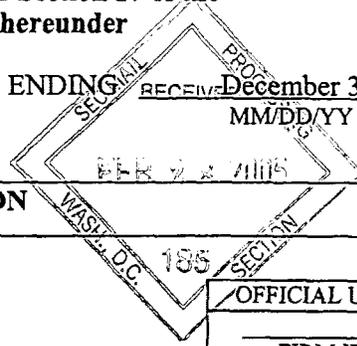
**ANNUAL AUDITED REPORT  
FORM X-17A-5  
PART III**

SEC FILE NUMBER
8-20746

FACING PAGE

**Information Required of Brokers and Dealers Pursuant to Section 17 of the  
Securities Exchange Act of 1934 and Rule 17a-5 Thereunder**

REPORT FOR THE PERIOD BEGINNING January 1, 2004 AND ENDING December 31, 2004  
MM/DD/YY MM/DD/YY



**A. REGISTRANT IDENTIFICATION**

NAME OF BROKER - DEALER:

David Lerner Associates, Inc.

ADDRESS OF PRINCIPAL PLACE OF BUSINESS: (Do not use P.O. Box No.)

477 Jericho Turnpike

(No. and Street)

Syosset

(City)

New York

(State)

11791

(Zip Code)

NAME AND TELEPHONE NUMBER OF PERSON TO CONTACT IN REGARD TO THIS REPORT

Alan Chodosh

(516) 390 5525

(Area Code - Telephone No.)

**B. ACCOUNTANT IDENTIFICATION**

INDEPENDENT PUBLIC ACCOUNTANT whose opinion is contained in this Report\*

Deloitte & Touche LLP

(Name - if individual, state last, first, middle name)

Two World Financial

New York

New York

10281-1414

(Address)

(City)

(State)

(Zip Code)

CHECK ONE:

Certified Public Accountant

Public Accountant

Accountant not resident in United States or any of its possessions.

PROCESSED

MAR 17 2005

THOMSON FINANCIAL

FOR OFFICIAL USE ONLY

\*Claims for exemption from the requirement that the annual report be covered by the opinion of an independent public accountant must be supported by a statement of facts and circumstances relied on as the basis for the exemption. See section 240.17a-5(e)(2).

TJH 3/14

AFFIRMATION

I, Alan P. Chodosh affirm that, to the best of my knowledge and belief, the accompanying financial statements and supplemental schedules pertaining to the firm of David Lerner Associates, Inc. (the "Company"), for the year ended December 31, 2004, are true and correct. I further affirm that neither the Company nor any officer or director has any proprietary interest in any account classified solely as that of a customer.

Alan P. Chodosh February 22, 2005  
Signature Date

Chief Financial Officer  
Title

DARLEEN BRICE  
NOTARY PUBLIC, State of New York  
No. 01 BR6045820  
Qualified in Queens County 05  
Commission Expires July 31, 20

Subscribed and sworn to before me on  
this 22<sup>th</sup> day of February 2005

Darleen Brice  
Notary Public



## INDEPENDENT AUDITORS' REPORT

To the Board of Directors of, and Stockholder of, David Lerner Associates, Inc.

We have audited the accompanying statement of financial condition of David Lerner Associates, Inc. (the "Company") as of December 31, 2004, that you are filing pursuant to Rule 17a-5 under the Securities Exchange Act of 1934. This financial statement is the responsibility of the Company's management. Our responsibility is to express an opinion on this financial statement based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such statement of financial condition presents fairly, in all material respects, the financial position of the Company at December 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

*Deloitte & Touche LLP*

February 22, 2005

# DAVID LERNER ASSOCIATES, INC.

## STATEMENT OF FINANCIAL CONDITION DECEMBER 31, 2004

---

### ASSETS:

CASH	\$ 8,525,480
CASH SEGREGATED UNDER FEDERAL AND OTHER REGULATIONS	2,519,312
CASH DEPOSITED WITH CLEARING ORGANIZATIONS	935,000
RECEIVABLES FROM:	
Customers	8,857,695
Brokers and dealers	4,116,796
Related parties	869,361
SECURITIES OWNED, AT FAIR VALUE	21,526,384
FURNITURE, EQUIPMENT AND LEASEHOLD IMPROVEMENTS AT COST, LESS ACCUMULATED DEPRECIATION OF \$3,135,668	1,843,510
OTHER ASSETS	<u>2,274,051</u>
TOTAL	<u>\$ 51,467,589</u>

### LIABILITIES AND STOCKHOLDER'S EQUITY :

PAYABLES TO:	
Customers	\$ 1,531,599
Brokers and dealers	184,040
SECURITIES SOLD, NOT YET PURCHASED, AT FAIR VALUE	6,828,871
COMMISSIONS PAYABLE	3,573,852
ACCOUNTS PAYABLE AND ACCRUED EXPENSES	<u>9,925,387</u>
	<u>22,043,749</u>
STOCKHOLDER'S EQUITY:	
Common stock, no par value; authorized 200 shares, 10 shares outstanding	5,000
Additional paid-in capital	952,370
Retained earnings	<u>28,466,470</u>
Total stockholder's equity	<u>29,423,840</u>
TOTAL	<u>\$ 51,467,589</u>

See notes to Statement of Financial Condition

# DAVID LERNER ASSOCIATES, INC.

## NOTES TO STATEMENT OF FINANCIAL CONDITION AS OF DECEMBER 31, 2004

---

### 1. INTRODUCTION, BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

David Lerner Associates, Inc. (the "Company") is a registered broker-dealer with the Securities and Exchange Commission and is a member of the National Association of Securities Dealers, Inc. The Company, headquartered in Syosset, New York, primarily conducts business with retail customers at branch offices in the east coast of the United States of America.

Customers' securities transactions are recorded on a settlement date basis with related commission income and expenses reported on a trade date basis. Purchases and sales of proprietary financial instruments as well as commission revenues and related expenses are recorded on a trade date basis.

Securities owned and securities sold, not yet purchased ("financial instruments"), are recorded at fair value. The fair value of financial instruments is generally based on observable market prices.

Depreciation is provided on a straight-line basis using an estimated useful life of five years. Leasehold improvements are amortized over the lesser of the economic useful life of the improvement or the term of the lease.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

In December, 2003, the FASB issued FIN 46R, '*Consolidation of Certain Variable Interest Entities – an interpretation of ARB No. 51.*' Which further clarifies FIN46 issued on January 17, 2003. FIN46R clarifies when an entity should consolidate another entity known as a Variable Interest Entity (VIE), more commonly referred to as special purpose entity or SPE. A VIE is an entity in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties, and may include many types of SPE's. FIN46R requires that an entity shall consolidate a VIE if that entity has a variable interest that will absorb a majority of the VIE's expected losses if they occur, receive a majority of the VIE's expected residual returns if they occur, or both.

FIN46R does not apply to certain qualifying SPEs (QSPEs), the accounting for which is governed by SFAS No 140. '*Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*'. FIN 46R is effective for newly created VIEs beginning December 31, 2003 and for existing VIEs as of the first annual period beginning after December 15, 2004.

On January 1, 2004, the Company adopted FIN46R for VIEs created after December 31, 2003. The effect of adopting FIN46R for VIEs created after December 31, 2003, did not have a material effect on the statement of financial condition. The Company will adopt FIN46R on January 1, 2005 for VIEs in which it holds a variable interest that it acquired before December 31, 2003. The impact of adopting FIN46R in full is not expected to be material to the financial statements.

## 2. RECEIVABLES FROM, AND PAYABLES TO, CUSTOMERS

Receivables from, and payables to, customers represent amounts due on cash and margin transactions. Securities owned by customers are held as collateral for receivables. Such collateral is not reflected in the statement of financial condition.

At December 31, 2004, the fair value of securities received as collateral where the company was permitted to sell or repledge the securities was \$1,284,865 and the fair value of the portion that had been sold or repledged was \$1,284,865.

## 3. RELATED PARTY TRANSACTIONS

The Company is wholly owned by David Lerner (the "Stockholder").

The Company provides administrative services and office space to an affiliate, SRLA, Inc. ("SRLA") owned by David Lerner Organization, which is owned by a relative of the Stockholder. In addition, the Company, SRLA and various other affiliates (controlled by the Stockholder) loan and borrow funds among the related parties.

At December 31, 2004, the receivables from related parties were as follows:

DSD Realty, LLC	\$ 211,124
HSS Realty, LLC (formerly known as David Lerner Realty)	271,779
Other	<u>386,458</u>
Total receivables from related parties	<u>\$ 869,361</u>

Pursuant to a lease extension agreement, entered into on December 5, 2001, between the Company and HSS Realty, LLC (an LLC owned by the Stockholder), the Company is liable for rental charges equal to the higher of the market rent or the monthly debt service costs of the indebtedness relating to the building occupied by the Company and its affiliates (see Note 8). The indebtedness matures on December 5, 2011. The lease terminates on December 31, 2011.

## 4. SECURITIES OWNED AND SECURITIES SOLD, NOT YET PURCHASED

Securities owned and securities sold, not yet purchased, consist of the following:

	Owned	Sold, Not Yet Purchased
Mortgage-backed securities	\$ 11,441,119	\$ 6,583,076
State and municipal obligations and other non-equities	8,739,043	245,795
Equities	1,346,222	-
Total	<u>\$ 21,526,384</u>	<u>\$ 6,828,871</u>

## 5. FURNITURE, EQUIPMENT AND LEASEHOLD IMPROVEMENTS

At December 31, 2004, furniture, equipment and leasehold improvements consist of the following:

Furniture and fixtures	\$ 2,431,433
Data processing equipment	950,587
Leasehold improvements	750,038
Telephone equipment	626,709
Automobiles	<u>220,411</u>
Total	4,979,178
Less accumulated depreciation and amortization	<u>3,135,668</u>
Furniture, equipment and leasehold improvements - net	<u>\$ 1,843,510</u>

## 6. OTHER ASSETS

At December 31, 2004, other assets consist of the following:

Prepaid expenses	\$ 993,283
Commissions receivable	438,400
Deferred compensation asset	353,194
Interest and dividend receivable	208,470
Employee advances and investment counselors' advances receivable	109,228
Other	<u>171,475</u>
Total other assets	<u>\$ 2,274,050</u>

## 7. EMPLOYEE BENEFITS

The Company sponsors a 401(k) plan (the "Plan") for the benefit of all full-time employees, after they have completed one year of service. The Company matches twenty-five percent of employee contributions up to \$1,500. Employees are fully vested in their own contributions. Company contributions vest twenty percent after two years of participation in the Plan and an additional twenty percent for each succeeding year, with full vesting after six years. It is the Company's policy to fund all amounts when due.

Beginning in 1987, qualified investment counselors became eligible to participate in a longevity bonus arrangement (the "Agreement"). A bonus of between 4 percent and 10 percent of annual compensation may be credited to their account, assuming certain minimum performance standards are achieved. The bonus is reduced by the Company's contribution to the investment counselors' 401(k) plan and is subject to a five-year vesting requirement. The amount of the bonus credited to an account for a given year will not be paid until five years later, providing the investment counselor is still employed by the Company. The Company may, at its sole discretion, terminate the Agreement at any time and each investment counselor would be entitled to bonus payments in accordance with the remaining terms of the Agreement (including the waiting period for payment).

The Company recognizes twenty percent of the gross liability in each of the five years, since the bonus amount is payable at the end of the fifth year. Adjustments to previous amounts recorded will be made in succeeding years based on investment counselors' terminations. The longevity bonus for the year ended December 31, 2004, which will be fully vested by the end of the fifth year, amounted to \$1,703,356 (total bonuses of \$1,725,003 less \$21,647 contributed to the 401(k) plan). The total unrecorded amount of \$2,672,672 is being recorded in equal installments over the years needed to record the full liability by the end of the respective fifth year. At December 31, 2004, the liability to investment counselors under the Agreement aggregated \$2,376,496 and is included in accrued expenses.

Effective as of January 1, 1998, the Company established the David Lerner Associates, Inc. Equity Participation Plan (the "EPP"). The EPP which is primarily for selected employees, has authorized 137,100 units representing ten percent of the Company's equity for grants to employees. The EPP's units are essentially the economic equivalent of shares in the Company. Subject to the terms of the EPP, after ten years, the holder of EPP units will be paid for the value of such units, over a five-year period. In addition, among the various provisions, the EPP provides for partial vesting beginning after five years from the date of grant and the option for the Grantee to extend the Grant at the end of the ten-year period. As of December 31, 2004, 115,450 EPP units are outstanding with a future value totaling \$1,846,300.

Beginning in 2001 the Company established a Deferred Compensation plan that allows a certain percentage of the Company's highly compensated employees to elect to defer each year the receipt of their bonus, currently up to \$10,000. As of December 31, 2004 the liability under the Deferred Compensation plan was \$353,194 and is included in accrued expenses.

The Company has a commitment to a former employee that provides annual payments of \$100,000, the present value of which, as of December 31, 2004, is \$1,173,338, and is recorded in 'Accounts Payable & Accrued Expenses' on the accompanying statement of financial condition.

## 8. COMMITMENTS AND CONTINGENT LIABILITIES

The Company is obligated under several noncancellable lease agreements primarily for the rental of office space. The lease agreements contain customary escalation clauses based principally upon real estate taxes, building maintenance and utility costs.

One of the above-mentioned leases is with an LLC owned by the Stockholder (see Note 3).

At December 31, 2004, minimum annual rental commitments, exclusive of common area charges, are as follows:

Year Ending December 31,	Amount
2005	\$ 1,292,917
2006	1,233,242
2007	1,149,804
2008	1,141,572
2009	951,177
Thereafter	<u>1,794,500</u>
Total	<u>\$ 7,563,212</u>

The Company has been named as a defendant in several claims and lawsuits arising from its securities business. Certain of the legal actions include claims for compensatory and/or punitive damages or claims for indeterminate amounts of damages. The Company is also involved in other reviews, investigations and proceedings by self regulatory agencies (both formal and informal) regarding the Company's business activities, certain of which could result in adverse judgments, settlements, fines or penalties. Management of the Company, based on discussions with legal counsel, believes that these actions are adequately provided for, and that their resolution will not have a material adverse effect on the financial condition of the Company.

## **9. GUARANTEES**

FASB Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others," requires the Company to disclose information about its obligations under certain guarantee arrangements. FIN 45 defines guarantees as contracts and indemnification agreements that contingently require a guarantor to make payments to the guaranteed party based on changes in an underlying related to an asset, liability or equity security of a guaranteed party. FIN 45 also defines guarantees as contracts that contingently require the guarantor to make payments to the guaranteed party based on another entity's failure to perform under an agreement as well as indirect guarantees of the indebtedness of others.

The Company is a member of a U.S. exchange and clearinghouse that trade and clear securities contracts. Associated with its membership, the Company may be required to pay a proportionate share of the financial obligations of another member who may default on its obligations to the exchange or the clearinghouse. While the rules governing different exchange or clearinghouse memberships vary, in general the Company's guarantee obligations would arise only if the exchange or clearinghouse had previously exhausted its resources. In addition, any such guarantee obligation would be apportioned among the other non-defaulting members of the exchange or clearinghouse. Any potential contingent liability under these membership agreements cannot be estimated. The Company has not recorded any contingent liability in the financial statements for these agreements and believes that any potential requirement to make payments under these agreements is remote.

## **10. NET CAPITAL REQUIREMENTS**

The Company is subject to the Uniform Net Capital Rule (Rule 15c3-1) under the Securities Exchange Act of 1934, which requires the maintenance of minimum net capital. The Company has elected to use the alternative method, permitted by the rule, which requires that the Company maintain minimum net capital, as defined, equal to the greater of \$250,000 or 2 percent of aggregate debit balances arising from customer transactions, as defined. (The Net Capital Rule of the New York Stock Exchange also provides that equity capital may not be withdrawn or cash dividends paid if resulting net capital would be less than 5 percent of aggregate debits.) At December 31, 2004, the Company had net capital of \$24,047,106 which was 280 percent of aggregate debit balances and \$23,797,106 in excess of required net capital.

## **11. INCOME TAXES**

The Company has elected to be taxed as an S corporation under the Internal Revenue Code. Accordingly, federal taxable income is reported separately by the Stockholder. The provision for income taxes for the year ended December 31, 2004 represents amounts provided for those states that impose a tax on S corporations and for those states that do not recognize S corporation status.

## **12. FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK**

As a securities broker, the Company is engaged in various brokerage activities servicing a diverse group of domestic corporations, institutional and individual investors and other brokers and dealers. All of the Company's transactions are collateralized and are executed with, and on behalf of, such clients. If a client's transaction does not settle because of the failure to perform by either the client or the counterparty, the Company may be required to discharge the obligation of the nonperforming party. The Company may incur a loss where the market value of a security rises and either the party from whom the Company has purchased the security does not make delivery, or where the Company has sold securities that it has not yet purchased.

The Company does not anticipate nonperformance by clients or counterparties in the above situations. The Company's policy is to monitor its market exposure and counterparty risk. In addition, the Company has procedures in place which are designed to monitor the credit worthiness of each client and counterparty with which it conducts business.

## **13. FAIR VALUE DISCLOSURES**

Due to the nature of its operations, substantially all of the Company's assets are comprised of cash, receivables from brokers and dealers, customers and related parties, and securities owned. The carrying amounts of the receivables are a reasonable estimate of fair value. Similarly, substantially all of the Company's liabilities arise from, payables to brokers and dealers, and customers, securities sold, not yet purchased, and other short-term liabilities. The payables are short-term in nature and the carrying amounts are a reasonable estimate of fair value.

\* \* \* \* \*

February 22, 2005

The Board of Directors of, and Stockholder of, David Lerner Associates, Inc.  
477 Jericho Turnpike  
Syosset, New York 11791

In planning and performing our audit of the financial statements of David Lerner Associates, Inc. (the "Company") for the year ended December 31, 2004 (on which we issued our report dated February 22, 2005), we considered its internal control, including the control activities for safeguarding securities, in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the Company's internal control.

Also, as required by Rule 17a-5(g)(1) under the Securities Exchange Act of 1934, we have made a study of the practices and procedures followed by the Company (including tests of compliance with such practices and procedures) that we considered relevant to the objectives stated in Rule 17a-5(g): (1) in making the periodic computations of aggregate debits and net capital under Rule 17a-3(a)(11) and the reserve required by Rule 15c3-3(e); (2) in making the quarterly securities examinations, counts, verifications and comparisons, and the recordation of differences required by Rule 17a-13; (3) in complying with the requirements for prompt payment for securities under Section 8 of Regulation T of the Board of Governors of the Federal Reserve System; and (4) in obtaining and maintaining physical possession or control of all fully paid and excess margin securities of customers as required by Rule 15c3-3.

The management of the Company is responsible for establishing and maintaining internal control and the practices and procedures referred to in the preceding paragraph. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control and of the practices and procedures, and to assess whether those practices and procedures can be expected to achieve the Securities and Exchange Commission's (the "Commission") above-mentioned objectives. Two of the objectives of internal control and the practices and procedures are to provide management with reasonable, but not absolute, assurance that assets for which the Company has responsibility are safeguarded against loss from unauthorized acquisition, use, or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit preparation of financial statements in conformity with accounting principles generally accepted in the United States of America. Rule 17a-5(g) lists additional objectives of the practices and procedures listed in the preceding paragraph.

Because of inherent limitations in any internal control or the practices and procedures referred to above, misstatements due to error or fraud may occur and not be detected. Also, projections of any evaluation of the internal control or of such practices and procedures to future periods are subject to the risk that they may become inadequate because of changes in conditions or that the degree of compliance with the practices or procedures may deteriorate.

Our consideration of the Company's internal control would not necessarily disclose all matters in the Company's internal control that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving the Company's internal control and its operation, including control activities for safeguarding securities, that we consider to be material weaknesses as defined above.

We understand that practices and procedures that accomplish the objectives referred to in the second paragraph of this report are considered by the Commission to be adequate for its purposes in accordance with the Securities Exchange Act of 1934 and related regulations, and that practices and procedures that do not accomplish such objectives in all material respects indicate a material inadequacy for such purposes. Based on this understanding and on our study, we believe that the Company's practices and procedures were adequate at December 31, 2004, to meet the Commission's objectives.

This report is intended solely for the information and use of management, the Board of Directors of, and Stockholder of, the Company, the Securities and Exchange Commission, the National Association of Securities Dealers, Inc., and other regulatory agencies that rely on Rule 17a-5(g) under the Securities Exchange Act of 1934 in their regulation of registered brokers and dealers, and is not intended to be and should not be used by anyone other than these specified parties.

Yours truly,

*Deloitte & Touche LLP*